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### **The Success Story of the Eurozone Crisis? Ireland's Austerity Measures**

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## Introduction

Recent financial press commentary paints a positive picture for Ireland's future. The tenth review by the European Union/European Central Bank/International Monetary Fund (EU/ECB/IMF - **the Troika**) of Ireland's progress concludes that: the gradual recovery is continuing and there have been further improvements in market conditions for the sovereign debt problem and the banks. Ireland has earned the nickname of the 'poster boy for austerity' for adhering to the Programme of Support from the Troika (Halpin and Papachristou, 2013). Ireland became the first Eurozone country to slide into recession in September 2008 with economic activity at its weakest in a quarter of a century (Smith, 2008). Now Ireland looks to become the first country to exit an EU-led bailout (Horta e Costa, 2013). There are differing views on this success.

"Ireland is setting standards and what has been done has been huge by any standards. More than two-thirds of the work has been done in terms of fiscal policies."

(Lagarde, 2013)

There has been heavy reliance on this external financial assistance programme, strict compliance with its terms and accompanying large cuts in public expenditure. The gravity of the situation has created an arena where financial cutbacks and austerity dominate.

"Like some terrible World War 1 conflict, we have sacrificed millions of lives to gain a metre of ground. Austerity is not working".

(Begg, 2013)

While there is evidence of some public sector reform progress there is also evidence of **limited** substantive reform to date. The financial straitjacket imposed by the EU/ECB/IMF agreement is a fundamental constraint on the actions of the State. However, the straitjacket provides legitimating support for government's programme of cutbacks in public services and new taxes. Nevertheless, as noted above, there is a mixed response to government attempts to rationalize its public services. The Government noted in its public sector reform programme that placing customer service at the heart of government is its focus (Department of Public Expenditure and Reform, 2011, p.3 ). However, the Government's claim to place the citizen at the centre of public sector reform efforts is somewhat disingenuous in view of funding cuts in health, education, social services and policing.

The corner has been turned in financial terms – the cost of issuing new government bonds has fallen and there have been some improvements in GDP growth rates. This paper sets out in the following sections the response of the Irish government to the impact of the financial crisis in the Eurozone. It focuses on the impacts of the Government response in shaping the future economic health of the country. The paper does not consider wider socioeconomic impacts of the actions of government – those are for future studies when these impacts are clear. The paper is structured as follows: a conceptual framework, the crisis, where we are now, public management reforms, budgets (cuts, cuts, cuts), and a conclusions section.

### **Conceptual framework**

Ireland is not alone in needing to make cutbacks. Other countries in the Eurozone area are faced with various fiscal and financial crisis. Fiscal crises culminate at a point that require decisions about cutbacks that are both politically sensitive and unpopular (Kickert, 2012). In Greece, Spain, Portugal and Italy national governments in their strategies of retrenchment failed to connect cutback management to ambitious administrative modernization programmes (Di Mascio and Natalini, 2013). Cutback management involves a choice between equity and efficiency concerns in choosing decision rules to allocate the cuts (Levine, 1978). There is a tension here between old style public administration values and those of the new public management (NPM) that gives different prominence to these two values. The pressure for cutbacks can come from two sources: external pressures or politicians' ideological convictions on the need for change (Dunsire and Hood, 1989). There is belief that financial and staffing pressures on public sector organisations will make them fitter, leaner and more efficient (Dunsire and Hood, 1989, p.186). Evolving control frameworks under NPM are weakening the priority given to equity concerns in policy design and implementation (Denhardt, 2004). A market-led approach to the business of government and the subsequent discharge of accountability solely in efficiency, effectiveness and responsiveness terms is considered deficient as a measure of accountability (Denhardt and Denhardt, 2000; Bardouille, 2000). This conflict between social democratic considerations and the drive for efficiencies is at the heart of recent debates over public sector management reforms. Suleiman (2003) suggests that NPM ideas aimed at addressing weaknesses in traditional bureaucracies in the pursuit of efficiency serve to undermine democracy itself. A concern with cutback management is the threat to the social contract – job security and other values – and the consequences of this for employee motivation (Pandey, 2010) as governments aim to reduce the size of public sectors. In the case of

Ireland, cutbacks have become necessary because of a crisis with multiple causes. The primary cause of the crisis and assistance secured to address it is examined in the next section.

## The crisis

On the last day of September 2008 the six domestic banks received government guarantees on all deposits and specific debt instruments until September 2010 subsequently extended until its removal on 28<sup>th</sup> March 2013 (Honohan, 2009, Oireachtas, 2008). As the government struggled to recapitalize the banks the cost of government borrowing reached unsustainable highs - 14% in July 2011. For a more detailed review of the banking crisis, the sustainability of Irish debt and the fiscal policies that contributed to the crisis, see: Honohan (2010), Regling and Watson (2010), Bergin *et al.* (2011), McHale (2012) and Kane (2012). In November 2010 the Irish government formally sought external financial help. An €85 billion financial assistance programme was approved by the IMF in liaison with the ECB and European Commission (EU/ECB/IMF, 2010, p.8) in December 2010. The €85 billion Programme for Support involves €67.5 billion of external assistance and €17.5 billion of funds to be generated internally (see Table 1 below). This €67.5bn is a loan which must be repaid in full with interest.

**Table 1:** EU/ECB/IMF Programme of Financial Support

		billion	billion
External	European Financial Stability Mechanism (EFSM)	€22.5	€67.5
	IMF Extended Fund Facility	€22.5	
	European Financial Stability Fund (EFSF) and bilateral loans from the UK, Sweden and Denmark	€22.5	
Internal	National Pension Reserve Fund and other domestic cash resources	€17.5	€17.5
	Total		€85.0

Source: EU/ECB/IMF (2010)

The programme provided for up to €50bn in fiscal needs and up to €35bn in banking support measures between 2011 and the end of 2013. The programme requires actions to address fiscal consolidation, financial sector reforms, and structural reforms. Structural reforms are aimed at resource conservation and improving competition to drive economic recovery. These changes have had a range of impacts which will be reviewed in the next two sections.

## Where we are now

In this section the impact of the crisis on: economic growth, the extent of and cost of government borrowing, the government surplus/deficit and migration is explored. Gross Domestic Product in Ireland (at constant market prices) increased in 2011, for the first time in four years (see Table 2). Having peaked in 2007, the GDP growth rate was negative for the next three years. In 2011 the GDP growth rate was positive again at 1.6 per cent and marginally positive in 2012. However, on a seasonally adjusted basis, GDP (at constant market prices) for the fourth quarter of 2012 showed almost no change compared with the previous quarter and GDP decreased 0.6% in the first quarter of 2013 as compared with quarter four of 2012 (Central Statistics Office, 2013a).

**Table 2:** Irish GDP and GDP Growth Rates 2005-2011

Year	GDP	Growth in GDP %
2005	163.0	8.5
2006	177.7	9.0
2007	188.7	6.2
2008	178.9	-5.2
2009	161.3	-9.8
2010	156.5	-2.9
2011	159.0	+1.6
2012	160.2	+0.9

Source: Central Statistics Office (2012a, p.17-18) and (2013b).

General government consolidated gross debt as a percentage of GDP in Ireland declined from 31.9 per cent to 24.8 per cent over the 2002-2007 period but then increased steeply in 2008 to 44.2 per cent. The debt to GDP ratio has continued to increase strongly year-on-year since 2008 to stand at 117.6% of GDP by the end of 2012. The steep rise in this government debt to GDP ratio reflects two things: declining GDP in the years 2008 to 2010 and only modest growth in GDP since then as shown in Table 2; and additional borrowing annually as Government continues to spend more than it collects in taxes, thereby giving rise to the need to borrow to finance annual current expenditure. Ireland had the third highest debt to GDP ratio in the EU in 2011 behind Greece and Italy. The Eurozone 17 debt to GDP per cent over the period 2002 to 2008 remained close to 70 per cent before rising over the last three years to stand at 87.2 per cent in 2011 (Eurostat, 2011). It is anticipated that Ireland's debt/GDP ratio will peak at 120.3 per cent in 2013 before falling to 117.4 per cent in 2015 (Department of Finance, 2012). Table 3 shows

Ireland's deficit has been declining as a percentage of GDP. For 2011 it was 9.4 per cent well below the EU/ECB/IMF Programme target for 2011 of 10.6 per cent (Department of Finance, 2012). EU/ECB/IMF Programme targets were also reached in 2012.

**Table 3:** Deficit as a percentage of GDP

Year	%	actual / target
2009	11.5	actual
2010	10.9	actual
2011	9.4	actual (target 10.6%)
2012	7.6	actual (target 8.6%)
2013	7.5	budget
2014	4.8	budget
2015	2.8	budget

Source: Central Statistics Office (2012a) and (Eurostat, 2013).

The cost of funding public services has also been affected. The yield on Irish government bonds is now at a level 3.8 per cent having peaked at 14 per cent in mid-2011 (Hancock, 2013). There was a more pronounced decline in yields on shorter maturities (National Treasury Management Agency, 2012, p.9). This decline in bond yields strengthens the State's chances of a full return to the bond markets and emerging from the bailout programme in late 2013 without requiring further significant financial support.

Net migration statistics form a part of the Irish crisis story. Numbers emigrating from Ireland started to increase sharply from 2005 and numbers leaving Ireland have continued to increase (see Table 4) thus masking a bigger problem in unemployment statistics since 2009. Unemployment was 6.4% in 2008 and had increased to 14.7% in 2012 although preliminary seasonally adjusted numbers for 2013 show an improvement at 13.7% (Central Statistics Office, 2013b). Emigration in any single year in the previous ten years had not exceeded 31,500 people with average emigration of 28,400 people in the ten years to 2004. In contrast, the number of immigrants peaked in 2007 and fell sharply for the next three years to reflect a more typical pattern of 50,700 immigrants on average per annum over the ten years prior to 2004.

**Table 4:** Net Migration Ireland 2004 – 2012 (000s)

	2004	2005	2006	2007	2008	2009	2010	2011	2012
Immigration	58.5	84.6	107.8	151.1	113.5	73.7	41.8	53.3	52.7
Emigration	26.5	29.4	36.0	46.3	49.2	72.0	69.2	80.6	87.1
Net	32	55.1	71.8	104.8	64.3	1.6	-27.5	-27.4	-34.4

Source: Central Statistics Office (2012b, Table 1 )

However, further analysis of emigration statistics shows that Irish people emigrating accounted for less than 50% of total emigration until 2011 (52.1%) see Table 5 (Central Statistics Office, 2012b). From 2006 to 2012 other Europeans accounted for large numbers of emigrants from Ireland.

**Table 5:** Migration from Ireland by Nationality 2006-2012

	2006	2008	2010	2012
Irish	42.5%	26.7%	41.8%	53.4%
EU-27	40.3%	54.9%	44.8%	33.9%
Rest of World	17.2%	18.4%	13.4%	12.7%
Total	36,000	49,000	69,200	87,100

Central Statistic Office numbers show that the number of Europeans emigrating between 2006 and 2008 almost doubled and stayed at this level for the next four years reflecting the departure of many Eastern Europeans who had come to work in the construction and other sectors in the boom years. The impact of the crisis on economic and financial indicators and also on the human pattern of migration occurred alongside efforts to reform as well as to reduce the cost of public services.

### **Public sector expenditure reduction and reform**

In this section the impact of the crisis on public sector workers incomes, public service capacity, state assets and the opportunity for public sector reform is examined. Existing public sector workers have endured pay cuts with harsher cuts to be imposed on new recruits to the public sector - a clear instance of the equity/efficiency tension in cutback management choices as noted earlier by Levine (1978). Future recruits to the public sector may respond negatively to this reduced benefits contract – a concern raised by Pandey (2010). In March 2009, a pension levy of 7 per cent on average was applied to the



earnings of public servants (other than judges) (Oireachtas, 2009). In addition, a reduction in rates of pay and allowances took effect on January 1<sup>st</sup> 2010, and combined with the pension levy, resulted in an effective average reduction of 14 per cent in salaries of existing public sector staff as well as a pay freeze until 2014 (Irish Government, 2010b, European Commission Directorate-General for Economic and Financial Affairs, 2011, Oireachtas, 2009).

In June 2010, against a background of private sector wage cuts and redundancies, the government and public sector unions reached an agreement aimed at wide ranging reform of the public sector, increased flexibility and redeployment and reduced headcount on a voluntary basis. This Public Service Agreement 2010-2014 (Croke Park 1) is an agreement between the Irish Government and the Committee of the Irish Congress of Trade Unions which represents public sector workers to work together to change the way in which public services are managed and delivered so that both the cost of public services and the number of people working in the public service will fall significantly, yet continue to meet the need for services and improve the experience of service users. A national implementation body was established in July 2010 and is responsible for overseeing, driving and verifying progress on the implementation of the Croke Park Agreement across the public service and for the resolution of issues as they arise. In late June 2013 Croke Park 2, (also known as the Haddington Road Agreement) was agreed (Irish Government, 2013). This involved a further pay cut (of 5.5%) for public servants earning more than €65,000 per annum on their full salary and other measures aimed at delivering €1bn in further savings by 2016. Salary cuts increase progressively to the point of a 10% marginal reduction for those earning more than €185,000. An earlier version of this agreement had been rejected in Spring 2013. After the rejection of the Croke Park 2 Agreement by public sector trade unions, the Government passed emergency legislation which allowed it to impose pay cuts on higher earners (salaries greater than €65,000), suspend increments, and alter the terms and conditions of public sector workers for public service groups that decided not to sign up to Croke Park 2 (Oireachtas, 2013). The General Secretary of the Civil Public and Services Union noted that:

members had been left with 'Hobson's Choice' over the deal and that... the result could not be seen as an endorsement of the Haddington Road Agreement, but rather as a result forced by Government through intimidation and fear.

He noted that:

the passing of emergency legislation, with draconian ministerial powers to change the conditions of Government employees, had left members with a gun to their heads.

The Unite Union regional secretary at the biennial conference of the Irish Congress of Trade Unions described attacks on working people as a “war”, whilst at the same Congress union staff representing the Irish Nurses and Midwives union said that:

the Labour Party [coalition partners in government] must be told it could not leave power with the financial emergency legislation still on the statute books to be used as a weapon of mass destruction against workers by a future administration (Wall, 2013b).

A key objective of the Croke Park Agreements is to avoid the scale of industrial unrest which characterized Ireland in the 1980s. There have been indications of this in recent press reports (Wall, 2013a, Halpin, 2013).

Historically, Ireland has been slow to adopt public sector reforms although this changed somewhat with codification of NPM ideas in legislation which supported implementation of NPM principles under the Strategic Management Initiative in Ireland from the mid 1990s (Robbins and Lapsley, 2005). In a speech at the 15<sup>th</sup> International Research Society for Public Management Conference the newly elected Minister for Public Service Reform noted in April 2011 that there was now an opportunity to radically change what we do in the public service and that parts of the public sector are not fit for purpose and need reform (Minister for Public Expenditure Reform - Brendan Howlin, 2011). The newly formed Department of Public Expenditure and Reform established by legislation on July 6<sup>th</sup> 2011 is responsible for reducing public expenditure and leading public service reform under the terms of the Croke Park Agreement. Expenditure and reform in the title of the new Department convey a commitment by this Government to interlink these two elements. The Department of Public Expenditure and Reform and all government departments carried out comprehensive expenditure reviews (CERs) in 2011. These and future CERs are intended to become “the keystone of financial management” (Department of Public Expenditure and Reform, 2012a, p.12).

Since 2009, public sector workers have experienced cuts in salaries, cuts in staff numbers and signed two Public Service Agreements aimed at maintaining a stable industrial relations environment. In tandem with reductions in public service staff numbers, the newly formed Department of Public Expenditure and Reform has planned a programme of reform based on: a renewed focus on customer service, maximizing new and innovative service delivery channels, radically reducing costs to drive better value for money, organizing in new ways and increasing the focus on implementation and delivery (Department of Public Expenditure and Reform, 2011, p.3 ).

The Irish government has stayed firmly within guidelines adhering to the budget reduction terms of the EU/ECB/IMF bailout with a consequent reduction in public services, particularly health services. Ten of eleven quarterly reviews have taken place as of August 2013 and satisfactory progress has been reported (International Monetary Fund, 2012). Whilst public sector reform is an **element** of the reform package it appears that most attention has been on **budgetary reductions** with consequent decreases in organizational capacity. The range and quality of public services have been affected and reductions in budgets have been keenly felt in health and education. For instance, there has been in excess of a 12 per cent reduction over the three year period 2008 and 2011 of home help hours for an increasing number of primarily elderly, but also disabled citizens (Health Service Executive, 2011, Table 14). In the overall health sector staff numbers are required to decrease by 12.2% (net reduction of 12,400 staff) to achieve budgetary targets. To date net reductions of 10,000 staff have been made, many of these front line staff (Health Service Executive, 2013). Government policy statements articulating a renewed focus on customer service is at odds with the public's experience of policy impacts of cutbacks such as these – a case of inconsistency between policy and practice. This reduced service for vulnerable sections of the population raises concerns about equity and efficiency trade-offs, a concern raised by Denhardt (2004). The primacy of financial cutbacks is explained further in the next section.

### **Budgets – cuts, cuts, cuts**

A National Recovery Plan was published in November 2010. It outlined actions to implement a fiscal policy aimed at maintaining a government deficit at not more than 3% of GDP in line with the Stability and Growth Pact – the agreement between European member states to protect the European Economic and Monetary Union. The recovery plan included a €15 billion budgetary adjustment over the four year period 2011-2014. Budget 2011 (delivered in December 2010) was the first phase of implementation of this plan. Two-thirds of the adjustment (€10 billion) was to come from expenditure cuts, with one third (€5 billion) expected to be generated from increased government revenues. The public service pay bill had already been reduced by €1.4 billion in 2009 as a result of pay cuts and a pension levy now paid by employees. This was the first reduction in public sector pay since 1933 (Department of Public Expenditure and Reform, 2012b). As with the cuts in expenditure, on the revenue raising side forty per cent of the adjustment was frontloaded to the first year of the plan - 2011. On the revenue raising side the focus was on broadening the tax base, as in 2010, forty-five per cent of tax units paid no income tax (Irish Government, 2010a, p.89).

Budget 2011 delivered in December 2010 consisted primarily of the pay cuts outlined earlier for public servants, cuts in social protection payments and cuts in capital expenditure. Budget 2012 and 2013 consisted of a combination of increased taxation measures including a new property tax and cuts in funding for public services. Cuts in funding for health services for instance included: reductions in numbers of health service staff under the Employment Control Framework, savings in procurement, and savings in prescription drug payments through greater prescribing of generic drugs. Cuts in education included: cuts in capitation grants across a range of further and adult education courses, reduction in the student maintenance grant, and a reduction in the fund for students with disabilities.

## Conclusions

As noted by Dunsire and Hood (1989) the pressure for cutbacks may come from two sources. In advance of the request for external financial assistance from Europe the Irish government had already embarked on a series of cutbacks in three budgets during the fourteen months to December 2009. Further cutbacks came at the insistence of the Troika. Whilst in Greece, Spain, Portugal and Italy national governments in their strategies of retrenchment failed to connect cutback management to ambitious administrative modernization programmes (Di Mascio and Natalini, 2013), the response of the Irish Government was to prioritize cutbacks in public services and new taxes. The newly elected government (February 2011) established the Department of Public Expenditure **and** Reform in July 2011. The Cabinet Committee responsible for reviewing progress on the Public Sector Reform Plan consists of the most senior politicians and civil servants. The extent of public sector **reform** in its rationalization programme is distinct. In the Public Service Reform Plan issues of **efficiency** are raised nine times while equity is not mentioned at all. The discharge of accountability solely in efficiency, effectiveness and responsiveness terms is considered deficient as a measure of accountability (Denhardt and Denhardt, 2000; Bardouille, 2000). Suleiman (2003) suggests that NPM ideas aimed at addressing weaknesses in traditional bureaucracies in the pursuit of efficiency serve to undermine democracy itself. Whilst equity as a concern is not mentioned, democratic accountability concerns are considered six times in the reform plan indicating some sense of balance between managerial accountability and efficiency concerns on the one hand and democratic considerations on the other. However, whilst public sector reform has received some attention, the primary focus of government and civil servants has been on adherence to the EU/ECB/IMF programme.

Fiscal imbalances in Ireland, as elsewhere, have required cutbacks that have proven unpopular (Kickert, (2012). There are potential consequences arising from this element of cutback management in terms of employee motivation and commitment (Pandey, 2010). Net migration, since 2009, masks a larger unemployment problem. Evidence was provided earlier in the paper of the growing disquiet voiced at the biennial Irish Congress of Trade Union conference at salary cuts, changes in terms of employment and other public service cutbacks which impact on the organizational capacity of the public sector.

The EU/ECB/IMF bailout has come at a cost of reduced sovereign control. The loss of control of the Irish government over its own budgetary policy was highlighted in November 2011 when details of the Irish National Budget for 2012 were discussed by the Bundestag's Budget Committee in advance of being discussed in the Irish parliament. The Irish Budget 2012 blueprint had been given to the German Finance Ministry as part of the agreed quarterly reviews of Ireland's €85bn Troika Programme of Support. EU/ECB/IMF oversight will continue for years after Ireland exits the Programme of Support. Oversight of the country's budget will be a permanent feature under the EU's new regulations following the near collapse of the euro.

There are some positive developments. Compared with other Eurozone countries there is relative political stability in Ireland since the current government enjoys a substantial majority in Parliament. The second public service agreement has been reached, albeit after the threat of emergency legislation to facilitate implementation of salary cuts if it was not agreed. This second agreement contains the word stability in its title denoting the importance of industrial relations stability to facilitate economic recovery. These aspects of stability assist in boosting confidence in Ireland's economic future. Unemployment statistics for 2013 show an improvement for the first time in five years, although this masks growing net emigration numbers. Investor confidence has grown as evidenced by the decline in yields on long and short term Government bonds. Recent short-term and long-term bond offerings have been oversubscribed indicating a renewed interest and demand for Irish sovereign debt, which augurs well for future fundraising efforts as Ireland prepares to exit the Programme of Financial Support. Structural reforms are focused on maintaining flexibility in the labour market and enhancing competitiveness. Growth in economic activity depends on the availability of cheap finance to fuel economic demand. However, Ireland's economic fortunes depend in large part on revival of trading partner growth which recently (2013) has halted the faltering progress Ireland was making on GDP growth.

The Department of Public Expenditure and Reform is in its infancy. Some limited steps have been taken to link reforms with cutbacks. The Comprehensive Expenditure Review 2012-2014 implements commitments made in the Public Service Reform Plan. However, the focus is on identification of savings by reducing both the number of agencies and staff numbers – is this cutbacks or true reform? A further study of the impact of reforms will be needed to examine the influence of reforms on the public service experiences of the Irish public as these changes are embedded. The crisis has given Government the impetus to downsize the public sector through a range of cutbacks. The quarterly reviews within “the Troika Agreement” provide a framework for addressing long standing problems. The programme for future public service reform is now supported by new fiscal rules, a medium term expenditure framework underpinned by a regular comprehensive review process, updated and refocused Value for Money Reviews and a move to performance budgeting. All of these elements have undertones that reflect a concern with efficiencies. Overall, the impact of this Irish austerity programme is a reduction in the capacity of the public sector to deliver public services. The maxim of ‘more with less’ has a hollow ring in the context of public management challenges in this environment of austerity.

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